
# THE WRONG SLANT IN THE WEAKER RINGGIT DEBATE

TALK! of the week

# NEWSLETTER

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let's TALK!
without fear or favour...


# THE WRONG SLANT IN THE WEAKER RINGGIT DEBATE

**To your editor, Jamari Mohtar, currency fluctuations are a natural outcome of floating exchange rates, and should not be a cause for worry as compared to currency devaluation, or a stronger currency that can reduce export competitiveness and make imports cheaper, which will cause trade deficit to widen further, thus damaging export-dependent industries and eventually weakening the currency in a self-adjusting mechanism.**

- Malaysian jet setters will definitely welcome a stronger ringgit because that would make travel to Europe or the US inexpensive.
- But the downside is a strong currency can exert significant drag on the economy over the long term, as entire industries are rendered non-competitive and thousands of jobs are lost.
- While some might prefer a strong currency, a weak currency can result in more economic benefits.
- Hence, we can already see a common fallacy about exchange rates that say a "stronger" or "appreciating" currency must be better than a weaker or depreciating currency.
- After all, from the brief explanation above it is not that obvious "strong" is necessarily better than "weak".
- Even in military term, a "strong" army need not necessarily be invincible or a "strong" fighting force. Just look at the recent counter offensives by the "weak" army of Ukraine, which has caused the "stronger" Russian army to withdraw from Kharkiv helter-skelter.
- When a currency becomes stronger, all it means is it can purchase more of other currencies. So definitely it benefits some, not all, in the economy and, obviously it harms others.
- But do not let this confuse you. Stronger currencies is not necessarily better, it's just a different ballgame.
- With the price of a typical good or service, it is clear that higher prices benefit sellers and hurt buyers, while lower prices benefit buyers and hurt sellers.
- In the case of exchange rates, where the buyers and sellers are not always intuitively obvious, it is useful to trace through how different participants in the economy will be affected by a stronger or weaker currency.


# THE WRONG SLANT IN THE WEAKER RINGGIT DEBATE

- Consider, for example, the impact of a stronger ringgit on six different groups of economic actors:
  1. Malaysian exporters selling abroad;
  2. foreign exporters (that is, firms selling imports in the Malaysian economy);
  3. Malaysian tourists abroad;
  4. foreign tourists visiting Malaysia;
  5. Malaysian investors considering opportunities in other countries via foreign direct investment or portfolio investment; and
  6. foreign investors considering opportunities in the Malaysian economy.

- Figure 1 captures their reactions towards a stronger ringgit and a weaker ringgit respectively.

| Group | A stronger ringgit | A weaker ringgit |
|---|---|---|
| Malaysian exporting firm | ☹ | ☺ |
| Foreign firm exporting to Malaysia | ☺ | ☹ |
| Malaysian tourist abroad | ☺ | ☹ |
| Foreign tourist in Malaysia | ☹ | ☺ |
| Malaysian investor abroad | ☹ | ☺ |
| Foreign investor in Malaysia | ☺ | ☹ |

- Let's analyse first the case of a **stronger ringgit.**

- **Malaysian exporter (sad emoticon):** A stronger ringgit is a bane for a Malaysian exporter. A strong ringgit means that foreign currencies are correspondingly weak.

- When the exporter earns foreign currencies via export sales, and then converts them back to ringgit to pay workers, suppliers, and investors, the stronger ringgit means that the weaker foreign currency buys fewer ringgits, and the firm's profits (as measured in ringgit) fall.

- As a result, the firm may choose to reduce its exports, or it may raise its selling price, which will also tend to reduce its exports. In this way, a stronger currency reduces a country's exports, and hence it incurs a trade deficit, which will result in a negative balance of trade.

- **Foreign exporter (smiley emoticon):** For a foreign firm exporting to Malaysia, a stronger ringgit is a boon. Each ringgit earned through export sales, when traded back into the domestic currency of the exporting firm, will now buy more of the domestic currency than expected before the ringgit had strengthened.

- As a result, the stronger ringgit means the firm will earn higher profits than expected. The firm will then seek to expand its sales in the Malaysian economy, or it may reduce prices, which will also lead to expanded sales.

- In this way, a stronger ringgit means consumers will purchase more from foreign producers, expanding the country's level of imports.

- **Malaysian tourist (smiley):** For a Malaysian tourist abroad exchanging ringgit for the relevant foreign currency, a stronger ringgit is a benefit. The tourist receives more foreign currency for each ringgit, and thus the cost of the trip in ringgit is lower. When the ringgit is strong, it is a jolly good time for Malaysians to tour abroad.

- **Foreign visitors (sad):** For foreign visitors, the opposite holds true. A relatively stronger ringgit means their own currencies are relatively weaker, so that as they convert their own currency to ringgit, they have fewer ringgits than previously. When the ringgit is strong, it is not an especially good time for foreign tourists to visit Malaysia.


- **Overseas Malaysian investor (sad):** A stronger ringgit is a curse for a Malaysian investor who has already invested money in another country.

- The Malaysian investor abroad must first convert ringgits to a foreign currency for investment in the foreign country, and then later convert that foreign currency back to ringgits.

- If in the meantime the ringgit becomes stronger vis-à-vis the foreign currency, then when the investor converts back to ringgits, the rate of return on that investment will be less than originally expected at the time it was made.

- **Foreign investor in Malaysia (smiley):** However, a stronger ringgit is a blessing for a foreign investor putting monies into a Malaysian investment, as it will boost the returns of the said foreign investor.

- That foreign investor converts from his domestic currency to ringgits for investment in Malaysia, while later planning to switch back to his domestic currency.

- If, in the meantime, the ringgit grows stronger, then when the time comes to convert from ringgits back to the foreign currency, the investor will receive more foreign currency than expected at the time the original investment was made.

- Let's now analyse the case of a weaker ringgit, which is the situation now in Malaysia.

- **Malaysian exporter (smiley):** A weaker ringgit leads to an increase in Malaysian exports.

- **Foreign exporter (sad):** For a foreign exporter, the outcome is just the opposite. A weaker ringgit means that foreign currency is more expensive, which means that foreign goods are more expensive also. This leads to a decrease in Malaysian imports, which is bad for the foreign exporter.

- **Malaysian tourists (sad):** They face the same situation as a Malaysian importer, as a weaker ringgit means that their trip will cost more, since a given expenditure of foreign currency will take more ringgits. The result is that the Malaysian tourist may not stay as long abroad, and some may choose not to travel at all.

- **Foreign visitors (smiley):** For the foreign tourist in Malaysia, a weaker ringgit is a boon. It means their currency is worth more, so the cost of a trip to Malaysia will be less hefty. They may then choose to take longer trips to Malaysia, and more foreign tourists may decide to go for their vacations in Malaysia.

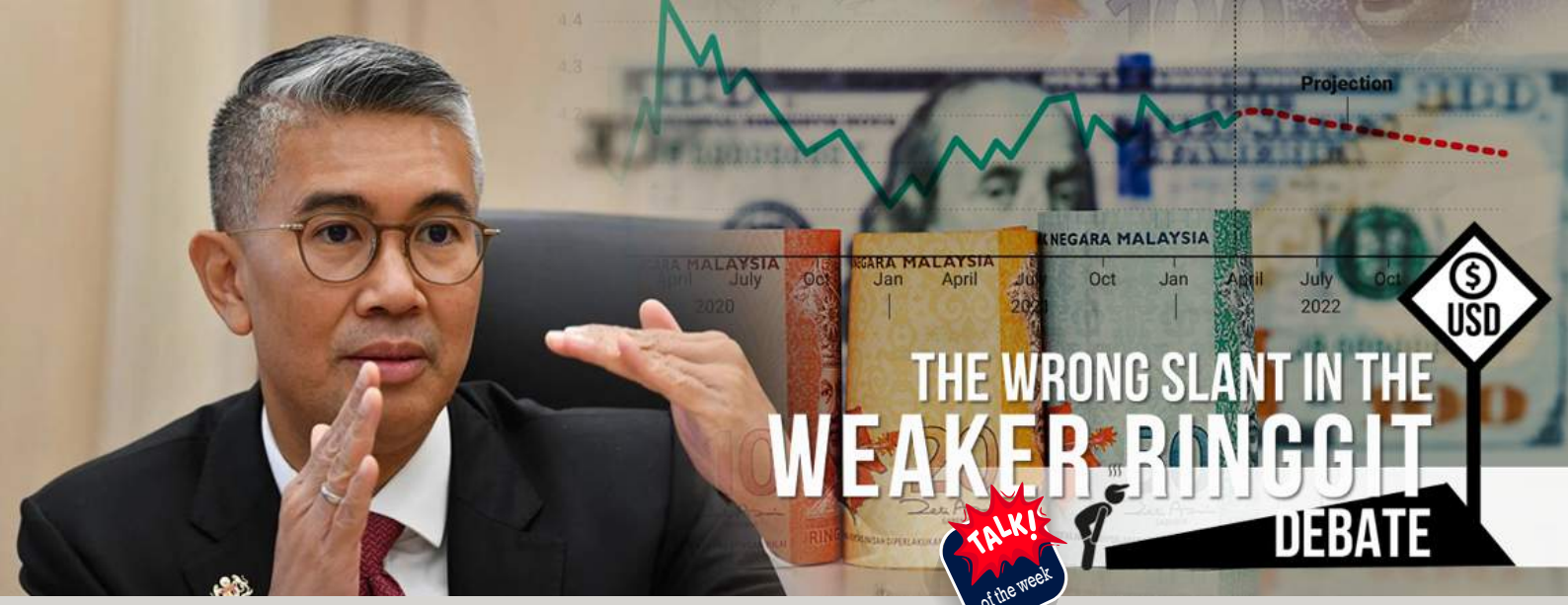
- **Overseas Malaysian investors (smiley):** A weaker ringgit is a boon for a Malaysian investor who has already invested money in another country.

- A Malaysian investor abroad must first convert the ringgit to a foreign currency for investment in that foreign country, and then later convert that foreign currency back to ringgit.

- If in the meantime the ringgit becomes weaker vis-à-vis the foreign currency, then when the investor converts back to ringgit, the rate of return on that investment will be more than originally expected at the time it was made.

- **Foreign investor in Malaysia (sad):** They face the same situation as a foreign exporter in the sense that they are purchasing a foreign asset.

- They will see a weaker ringgit as an increase in the "price" of investment, since the same number of ringgit will buy less foreign currency and thus less foreign assets. This should decrease the amount of Malaysian investment abroad.




# THE WRONG SLANT IN THE WEAKER RINGGIT DEBATE

TALK! of the week

- So what all this means is for a given weaker ringgit, three groups of economic actors experience bliss, while another three experience misery.

- The same groups that enjoy bliss with a regime of weaker ringgit will experience misery with a stronger ringgit and vice versa with the other three groups in the case of a stronger ringgit.

- So from the above explanation politicians who accused the government of not knowing what to do to "strengthen" the ringgit are barking up at the wrong tree.

- If the government listens to them, then what will happen is, assuming their recommendations strengthen the ringgit, what we will see is a change of position – the smiley economic actors will become miserable, and the miserable will become the smiley emoticons.

- Whether they realise it or not, these politicians are just playing the role of the rotten lobbyists ala the US political system. They work on behalf of the miserable i.e. the foreign exporters, the Malaysian tourist abroad and the foreign investors in Malaysia at the expense of the smiley actors i.e. Malaysian exporters, foreign tourists in Malaysia and Malaysian investors abroad (see Figure 1, page 4).

- Unless they can come up with proposals on how the miserable can be transformed into smiley actors with a stronger ringgit, without affecting the fate of those smiley actors who flourish under a weaker ringgit, their call for a stronger ringgit amount to nothing.

- The government correctly sees the weakening ringgit as a non-issue as it will not lead Malaysia to an economic crisis as Finance Minister Tengku Dato' Seri Zafrul Tengku Abdul Aziz puts it.

- Whatever the government does with the currency, some segments of the *rakyat* will benefit and some will suffer as explained above.

- The solution lies in mitigating the sufferings of those harmed by the weaker / stronger ringgit, and not in artificially appreciating / depreciating the ringgit.

- What these politicians don't see is that it is not the weaker ringgit that is the problem but inflation.

- It is fashionable nowadays in this era of financial crisis to see your country's currency stronger, and this has become somewhat populist, especially at a time of an election fever.

- If these politicians come into power with their own idea of a stronger ringgit while remaining disconnected to the real issue of a weaker ringgit vis-à-vis a stronger ringgit, the country will go down the drain.

- In economics, depreciation of currency that is 10% or less is an everyday occurrence that is not a cause for worry for as long as it does not take place on many consecutive days.

- Ditto with less than 20% depreciation, which could happen once in a while.

- But you've got to be very careful when there is a sudden 20% decline in the domestic currency because that is no longer a depreciation, but as good as a devaluation of the currency because it could lead to imported inflation for countries that are substantial importers.

- This is because a sudden 20% decline in the domestic currency could result in imports costing 25% more, as a 20% decline means a 25% increase is needed to get back to the original price point.


# THE WRONG SLANT IN THE WEAKER RINGGIT DEBATE

- Even before the ringgit weakened, the threat of an imported inflation is already there with the high energy and food prices brought about mainly by sanctions on Russia by the US and EU.

- So it is not the depreciation of the ringgit that should be our focus of attention as there is a self-adjusting mechanism in the foreign exchange market.

- Rather, what we should watch out is not to let the devaluation of the ringgit happens, and this is achieved by focussing our attention on the threat of imported inflation.

- One other thing the politicians clamouring for a stronger ringgit get it wrong is the slant of the story on the weaker ringgit.

- The slant of the story is not that the ringgit is weakening against all other currencies, but rather mainly with the US dollar, the reserve currency of the world.

- And the US like its allies in the EU is in a Catch-22 situation. The massive sanctions they imposed on Russia not only hurts Russia but boomerang to them as well in the form of an unprecedented spike in energy and food prices causing galloping inflation that was not seen in many years.

- This high inflation can only be tamed with higher interest rate and the US Federal Reserve (The Fed) is very focussed in sticking to aggressive rate hikes as inflation stays hot.

- The Fed is expected to deliver a third straight 75-basis point interest rate hike this week, if not more, after a US government report showed that consumer prices did not ease as expected in August and price pressures appeared to broaden.

- With an aggressive rate hikes approach, the US dollar is bound to appreciate again against all currencies in the coming days and weeks although the US is aware that such aggressive policies could result in the country going through a recession which will be contagious in spreading to other parts of the world.

- But this is another Catch-22 story that will unfold much later and it would be interesting to watch when the US will stop this aggressive rate hikes policy in order to prevent recession.

- Thus we can clearly see the angle or slant of the story as the ringgit weakens against the US dollar is then the story of almost all major currencies undergoing depreciation against the US dollar including the mighty Euro, the currency of the EU countries.

- And thus the issue becomes is Malaysia the worst affected country in term of currency depreciation against the US dollar?

- As pointed by Zafrul while the ringgit has depreciated by 7.5% against the US dollar since the beginning of 2022, many currencies in the region and developed countries have also fallen against the greenback.

- "For example, the Japanese yen has slid 19.2%, the lowest in 24 years; the pound sterling has dropped 14.4%, the lowest in 37 years; and the euro has weakened by 11.7%, the lowest in 20 years," Zafrul said in a video posted on his social media page.

- So Malaysia is doing well relative to all these countries as the ringgit's slide is the lowest among them all. Zafrul also stressed the ringgit has strengthened compared with the currencies of Malaysia's other trading partners.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TALK! of the week

- Among others, the ringgit has risen by 14.2% against the Japanese yen, 8.2% versus the pound sterling, 4.5% vis-a-vis the euro, 3.9% compared with the New Zealand dollar, and 7.2% against the South Korean won.

- "The important thing is, as an exporting country, the low ringgit against the US dollar has a positive effect on the country's export revenue.

- "So do not look at just one aspect. Ask Malaysian exporters, they are all happy as their exported products have become more competitive," he said.

- Additionally, economic fundamentals that have continued to strengthen are important in determining the robustness of the ringgit, the minister said.

- "What are the proofs (that our economy is on a solid footing)? Firstly, Malaysia's gross domestic product (GDP) has grown for three consecutive quarters.

- "The GDP grew by 3.6% in the fourth quarter of 2021, 5% in the first quarter of 2022 and 8.9% in the second quarter," he said.

- Zafrul said the country's unemployment rate of 3.7% in July 2022, the lowest since the Covid-19 pandemic hit the country, is further proof that the country is not experiencing an economic crisis.

- He also pointed to the Industrial Production Index, which rose by 12.5% year-on-year (y-o-y) in July 2022, and the sales value of the wholesale and retail trade which surged 41% to RM130.7 billion in the same month.

- "For the first seven months of this year alone, wholesale and retail trade was valued at RM882.1 billion, 19% higher than last year," he said.

- Zafrul also noted that the country's exports increased by 38% y-o-y to RM134.1 billion in July.

- He added that net foreign investment in the local stock market has amounted to more than RM8 billion and net retail investment has reached RM1.8 billion year-to-date.

- The country's inflation rate is also manageable at 2.8% for the first seven months of 2022 due to price control measures, particularly through the provision of subsidies of almost RM80 billion this year.

- "So, it makes no sense for some to say, despite these positive indicators, that we are in an economic crisis," Zafrul said.

- What was the reaction of these politicians who seems to be 'paralysed' by a weakened ringgit to Zafrul's statement?

- Contemptuously accusing Zafrul of downplaying the ringgit's slide, and warning him that a downtrend against the greenback would affect Malaysians as it would see an increase in the cost of imported food, as if Zafrul is too naïve not to know this.

- The problem of rising cost of imported food predates the current slide in the ringgit. In fact, the general problem of rising cost of living is a perennial problem starting back from BN's rule.

- Even during the short rule of Pakatan Harapan the problem was there with one think tank's head, Datuk Wira Dr Rais Hussin coining the term the *perut* economy (the stomach economy or bread and butter issues) because he was aghast at the slow pace of the PH government in addressing this issue.

- At least the Perikatan government led by Umno's Datuk Seri Ismail Sabri Yaakup has made an attempt to solve this rising cost of imported food by taking the long-term measure of being self-sufficient in the animal feed industry, which is one big reason why Malaysian poultry and livestock farming is a high cost industry that has to rely on imports of animal feed which is susceptible to currency fluctuations of the greenback.

- And please, no contemptuous complain for now on the issue because long term being long term, you won't see the results now.

- Even economists interviewed by Malaysiakini said the ringgit slide effect on daily life is minimal, although it's best to cut spending.


# ADVERTISEMENT

We all know that the pandemic has taken a toll on the livelihoods of many Malaysians. With the lockdown (a.k.a. MCO or Movement Control Order in Malaysia) lifted for inter-district and inter-state travels, and with domestic tourism in full swing since the success of the pilot project on the Langkawi travel bubble, rays of hope are in the offing for the economy to be healed, and we can therefore expect a good fourth quarter GDP growth that will propel the economy to perform better and better, albeit gradually.

But as in the nature of things, there will be a delayed effect in that some *rakyats* will continue to suffer from the economic impact of the pandemic in the sense that for them, especially for the vulnerable group, things will get worse before they get better. The Government, to its credit, is reaching out to this vulnerable group by pumping in more financial assistance, aiming to make Malaysia an attractive destination for foreign investors and to increase high value-added employment.

Some from the vulnerable group are enterprising enough to embrace the challenge by taking advantage of the burgeoning digital platforms where people are more and more beginning to do all sorts of things online (your Editor is no exception), including setting up businesses and working from their mobile phones, in order to make ends meet.

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# MITIGATING THE EFFECT OF A WEAKER RINGGIT ON THE SUFFERERS


- We have seen how the weaker ringgit has caused three groups of actors in the economy to suffer – the foreign firms exporting to Malaysia, Malaysian tourist abroad and the foreign investor in Malaysia.

- We leave the other three groups alone in their bliss with a weaker ringgit – the Malaysian exporters, foreign tourists in Malaysia and Malaysian investors abroad.

- This approach is better than the opposition's call for the government to tinker the exchange rate to make the ringgit stronger, which is a zero-sum game, as it will transform the misery of the sufferers into a state of bliss at the expense of those who are already in a blissful state with a weaker ringgit.

- Let's now focus on how the sufferings of the foreign firms exporting to Malaysia can be mitigated. When we talk about them, it includes their agents and distributors in Malaysia i.e. the local importers who also suffer.

- The Malaysian authorities could negotiate with them to diversify their exports to Malaysia by increasing the imports of goods/services that's crucial to Malaysia at competitive prices for example animal feeds while Malaysia is waiting for self-sufficiency in producing animal feeds.

- Ditto with the import of food and agricultural products at competitive prices that will enhance food security, and the import of raw materials for the manufacturing of high technology products.

- Since exports will flourish in a weaker ringgit environment, those local importers dealing with raw materials and products that are not crucial to Malaysia e.g. luxury goods/services should be encouraged and incentivised to become exporters of any goods/services that Malaysia's trading partners needed most.

- As for the sufferings of the Malaysian tourists abroad, this can be mitigated with the development of local tourist resorts that mimicked the overseas resorts such as a skiing resort with artificial snow.

- With such resort facilities, Malaysians then don't have to go for a hefty holiday experience abroad skiing in the snowy resort of Switzerland or the Italian Alps and Dolomites for the perfect mountain vacation with a weaker ringgit.

- They can go to this expensive holiday spots when the ringgit is stronger.

# MITIGATING THE EFFECT OF A WEAKER RINGGIT ON THE SUFFERERS

- Having holiday resorts that are adapted to the western environment will give the signals to more western tourists to come to Malaysia for a longer period for another purpose – saving hefty energy bills at home by leaving home for relatively longer period of vacation overseas at a time when energy prices are skyrocketing in the US and EU.

- Also Malaysian investors abroad who is in a blissful state with a weaker ringgit can diversify their investment in holiday resorts overseas and then give Malaysian tourists abroad a hefty discount to these places at a time when the ringgit is weaker.

- The misery of the last sufferer of a weaker ringgit – the foreign investor in Malaysia – can be mitigated by giving them a hefty incentive to invest in the high technology sector of Malaysia.

- Thus, a situation of a weaker ringgit is an opportunity to restructure the economy for a high technology and self-sufficient economy.
  Read more on currency fluctuations and their impact on the economy, and whether the weakening of ringgit against the greenback will lead to an economic crisis:

  Currency Fluctuations: How they Affect the Economy

  Ringgit versus US dollar: What we need to understand

  What a weak Ringgit means for Malaysia

  Ringgit heads to 24-year low on oil price slide

  Ringgit slips to new 24-year low against US dollar

  Malaysia not in an economic crisis despite Ringgit's value against US Dollar -- Tengku Zafrul

  Malaysia unlikely to slip into recession due to economic diversification, says Bursa chair

  Don't downplay ringgit's slide, Tengku Zafrul told

  Fed to stick to aggressive rate hikes as inflation stays hot

  Economists: Ringgit slide effect on daily life minimal, but best to cut spending

## THE CASE OF

# SINGAPORE WITH ITS STRONG CURRENCY

- In the 1960s and 1970s Singapore was the only industrial based country surrounded by the agricultural and commodities based economy of its neighbours.

- With its entrepot advantage still intact since colonial time, it went on an industrialization spree by welcoming multi-national companies (MNCs) to operate on its shores which was not fashionable at that time as most Asian countries resorted to import substitution to industrialise their economies.

- Furthermore for the newly independent Asian countries calling the foreign MNCs to operate in their countries smacked of neo-colonialism.

- Turned out, Singapore's approach was the better one and the country progressed with a relatively, not so much a strong currency, but a stable one with an industrialisation process that was very much labour intensive.

- When other countries copied the Singapore model, initially this lead to a stronger Singapore dollar because it still has the edge in attracting established MNCs.

- But we know from economics that if a strong currency is maintained, it will lead in the long run to an erosion of export competitiveness, thus damaging export-dependent industries which can exert significant drag on the economy over the long term, as entire industries are rendered non-competitive and thousands of jobs are lost.

- This scenario, however, did not happen to Singapore as its leaders then have the foresight to restructure its economy to move up the value added chain from a labour intensive industrial economy to a capital intensive industrialised economy during the 1980s and 1990s.

- The good thing about this strategy is Singapore never saw its neighbours then moving towards a labour intensive industry as a competitor but instead as complementing the city-state's move to a capital intensive industrial nation.

- It never resorted to beggar-thy-neighbour policies. The idea behind beggar-thy-neighbour policies is the protection of the domestic economy by reducing imports and increasing exports – usually achieved by encouraging consumption of domestic goods over imports using protectionist policies – such as import tariffs or quotas – to limit the amount of imports.

- It relocated its labour intensive industries to neighbouring countries and helped them in setting up industrial parks, along with its successful ambition implemented since the 1970s to make the country a vibrant international financial hub.

- With this restructuring of the economy, the Singapore dollar maintained its strong standing not only in comparison with the currencies of neighbouring countries but also with many currencies of the world.


## THE CASE OF
# SINGAPORE WITH ITS STRONG CURRENCY

- And when the neighbouring countries decided to move up the ladder in the value added chain by doing what Singapore has done in moving to a capital intensive industrial country, the republic once again restructure its economy into a high technology one, thereby maintaining its strong currency without affecting its export competiveness.

- It achieved this high-technology economy by making its economy a knowledge-based one.

- As neighbouring countries yet again move towards a high technology economy, Singapore is restructuring its economy to a service oriented one.

- Another factor that accounts for a strong Singapore dollar is when the republic chooses the exchange rate (rather than interest rates) as the principal tool of monetary policy.

- This is predicated on its small size and high degree of openness to trade and capital flows.

- A basic philosophy underlying Singapore's exchange rate policy is to preserve the purchasing power of the Singapore dollar in order to maintain confidence in the currency and preserve the value of workers' savings.

- Just as some of Singapore's particular characteristics necessitate a unique monetary policy framework, there are several structural factors, which have allowed the exchange rate to function effectively as an intermediate target of monetary policy.

- First, the country's high savings rates in the public sector due to the government's budgetary surpluses, along with the contribution of companies and households to the mandatory CPF, have led to the continual withdrawal of liquidity from the banking system.

- The Monetary Authority of Singapore (MAS) accordingly injects liquidity into the market by selling Singapore dollars and buying US dollars to offset government and CPF flows.

- Secondly, MAS has gained credibility through its pre-emptive and effective policy decisions by its single-mindedness and discipline in focusing on medium-term inflation trends, coupled with its robust reserves, have earned the trust of the market and public.

- It adopts a medium- to long-term orientation in formulating monetary policy, anticipating a six- to nine-month lag between implementation and impact.

- This medium-term orientation has helped to reduce the volatility of the exchange rate, anchoring the economy and providing certainty for businesses and households.

- Finally, the effectiveness of Singapore's exchange rate policy is due to the broader framework that its monetary policy is part of. Monetary policy does not work in a vacuum. Instead, it is situated within a wider framework of sound and consistent policies, including flexible prices and wages, a deep and efficient financial market, a robust corporate sector and prudent fiscal policy.

- In Singapore, the close coordination between fiscal policy and monetary policy has successfully ensured macroeconomic stability in the past decades, including meeting the challenges of past and recent financial crises.

- Singapore also provides a reason why having a stronger currency is not necessarily better.


# THE CASE OF SINGAPORE WITH ITS STRONG CURRENCY

- The MAS has reported a net loss of S$7.4 billion in the financial year ended 31 March 2022. Additionally, Singapore's official foreign reserves (OFR) also recorded a net loss of S$4.7 billion for the same financial year.

- The MAS OFR is held in foreign currencies, and according to MAS, three-quarter of the OFR is held in USD, euro, yen and pound, majority of which is held in US dollar.

- A Channel NewsAsia report back in July said the Singapore dollar is performing well against the euro and pound, and is at an all-time high against the yen.

- As MAS report its profit in Singapore dollar, the appreciation of its currency means it'll get lesser Singapore dollars when translating (converting) the foreign currency into the local currency.

- This is the main reason why the OFR saw a net loss of S$4.7 billion despite making a profit of S$4 billion in foreign investments.

- In turn, this is the reason MAS would not be contributing to Singapore's Consolidated Fund this year. However, it is considered as a short-term loss.

- This is the first time it has not contributed in 2 years, as MAS had contributed S$2.17 billion in FY 2019/20 and S$1.07 billion in FY 2020 / 21.

- The Consolidated Fund is just like a bank account held by the Singapore Government, of which revenues are channelled towards and out of which Government expenditures are spent.

- In years of net profits, the contribution for each financial year will be paid over a period of three years to ensure the stability of the government budget.

- Even though MAS will not be contributing to the Consolidated Fund, the Government will still receive S$1.1 billion due to the previous years' profits.

- Your editor is not trying to say that Singapore's policy of maintaining a strong currency is a bad one. Overall this policy has brought tremendous benefits to the country.

- It is how the negative effect of a stronger/weaker currency is mitigated that matters and according to many analysts, with a strong reserve to begin with, built up through the years, Singaporeans would not be affected that much by the loss of its OFR due to a stronger currency.

- As I said earlier, a stronger or weaker currency is a different ballgame, and neither is intrinsically good or bad.

Read more on Singapore's stronger currency, the exchange rate (rather than interest rates) as the principal tool of monetary policy, and Singapore recorded a net loss of S$4.7 billion in official foreign reserves (OFR) due to a stronger Singapore dollar:

**An exchange-rate-centred monetary policy system: Singapore's experience**

**MAS posts $7.4b annual loss, weighed down by stronger Singdollar amid soaring inflation**

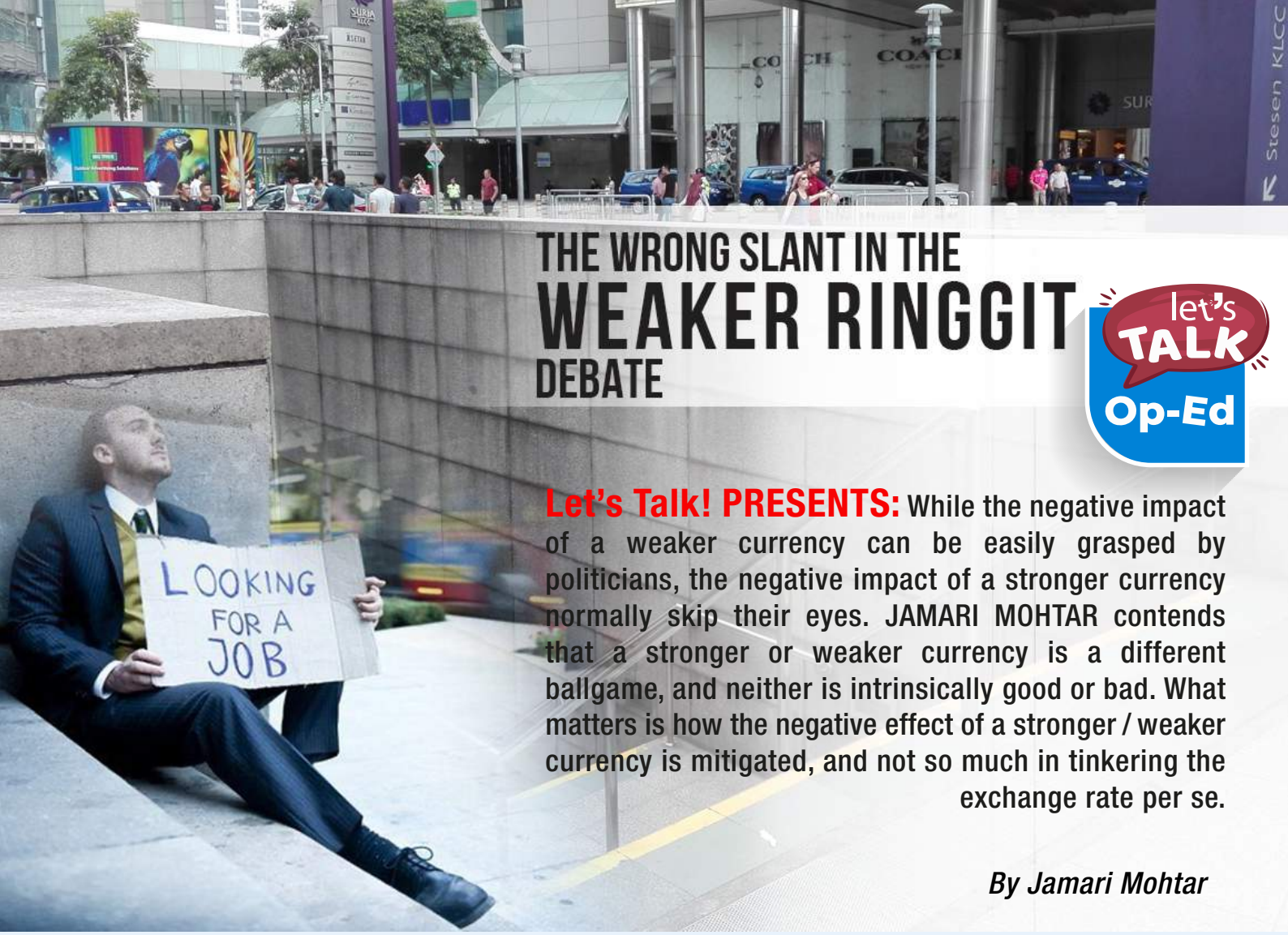
**Singdollar up against most major currencies – why and what that means for you**

**MAS posts S$7.4b loss, makes no contribution to Consolidated Fund in FY21 / 22**

**MAS's move to strengthen SGD unlikely to be 'game changer' for USD / SGD upward trend: analysts**

**Jury is out on whether MAS will tighten monetary policy again in October**

**Reply to Parliamentary Questions on implication of $7.4 billion loss reported by Monetary Authority of Singapore**




# THE WRONG SLANT IN THE WEAKER RINGGIT DEBATE

let's TALK Op-Ed

**Let's Talk! PRESENTS:** While the negative impact of a weaker currency can be easily grasped by politicians, the negative impact of a stronger currency normally skip their eyes. JAMARI MOHTAR contends that a stronger or weaker currency is a different ballgame, and neither is intrinsically good or bad. What matters is how the negative effect of a stronger / weaker currency is mitigated, and not so much in tinkering the exchange rate per se.

*By Jamari Mohtar*

Malaysian jet setters will definitely welcome a stronger ringgit because that would make travel to Europe or the US inexpensive. But the downside is a strong currency can exert significant drag on the economy over the long term, as entire industries are rendered non-competitive and thousands of jobs are lost.

While some might prefer a strong currency, a weak currency can result in more economic benefits. Hence, we can already see a common fallacy about exchange rates that say a "stronger" or "appreciating" currency must be better than a weaker or depreciating currency.

After all, from the brief explanation above it is not that obvious "strong" is necessarily better than "weak".

Even in military term, a "strong" army need not necessarily be invincible or a "strong" fighting force. Just look at the recent counter offensives by the "weak" army of Ukraine, which has caused the "stronger" Russian army to withdraw from Kharkiv helter-skelter.

When a currency becomes stronger, all it means is it can purchase more of other currencies. So definitely it benefits some, not all, in the economy and, obviously it harms others.

But do not let this confuse you. Stronger currencies is not necessarily better, it's just a different ballgame.

With the price of a typical good or service, it is clear that higher prices benefit sellers and hurt buyers, while lower prices benefit buyers and hurt sellers.
In the case of exchange rates, where the buyers and sellers are not always intuitively obvious, it is useful to trace through how different participants in the economy will be affected by a stronger or weaker currency.

Consider, for example, the impact of a stronger ringgit on six different groups of economic actors:

1. Malaysian exporters selling abroad;
2. foreign exporters (that is, firms selling imports in the Malaysian economy);
3. Malaysian tourists abroad;
4. foreign tourists visiting Malaysia;
5. Malaysian investors considering opportunities in other countries via foreign direct investment or portfolio investment; and
6. foreign investors considering opportunities in the Malaysian economy.

# THE WRONG SLANT IN THE WEAKER RINGGIT DEBATE

let's TALK Op-Ed

Figure 1 captures their reactions towards a stronger ringgit and a weaker ringgit respectively.

| Group | A stronger ringgit | A weaker ringgit |
|---|---|---|
| Malaysian exporting firm | ☹ | ☺ |
| Foreign firm exporting to Malaysia | ☺ | ☹ |
| Malaysian tourist abroad | ☺ | ☹ |
| Foreign tourist in Malaysia | ☹ | ☺ |
| Malaysian investor abroad | ☹ | ☺ |
| Foreign investor in Malaysia | ☺ | ☹ |

Let's analyse the case of a stronger ringgit.

**Malaysian exporter (sad emoticon):** A stronger ringgit is a bane for a Malaysian exporter. A strong ringgit means that foreign currencies are correspondingly weak.

When the exporter earns foreign currencies via export sales, and then converts them back to ringgit to pay workers, suppliers, and investors, the stronger ringgit means that the weaker foreign currency buys fewer ringgits, and the firm's profits (as measured in ringgit) fall.

As a result, the firm may choose to reduce its exports, or it may raise its selling price, which will also tend to reduce its exports. In this way, a stronger currency reduces a country's exports, and hence it incurs a trade deficit, which will result in a negative balance of trade.

**Foreign exporter (smiley emoticon):** For a foreign firm exporting to Malaysia, a stronger ringgit is a boon. Each ringgit earned through export sales, when traded back into the domestic currency of the exporting firm, will now buy more of the domestic currency than expected before the ringgit had strengthened.

As a result, the stronger ringgit means the firm will earn higher profits than expected. The firm will then seek to expand its sales in the Malaysian economy, or it may reduce prices, which will also lead to expanded sales.

In this way, a stronger ringgit means consumers will purchase more from foreign producers, expanding the country's level of imports.

**Malaysian tourist (smiley):** For a Malaysian tourist abroad exchanging ringgit for the relevant foreign currency, a stronger ringgit is a benefit. The tourist receives more foreign currency for each ringgit, and thus the cost of the trip in ringgit is lower. When the ringgit is strong, it is a jolly good time for Malaysians to tour abroad.

**Foreign visitors (sad):** For foreign visitors, the opposite holds true. A relatively stronger ringgit means their own currencies are relatively weaker, so that as they convert their own currency to ringgit, they have fewer ringgits than previously. When the ringgit is strong, it is not an especially good time for foreign tourists to visit Malaysia.

**Overseas Malaysian investor (sad):** A stronger ringgit is a curse for a Malaysian investor who has already invested money in another country.

# THE WRONG SLANT IN THE WEAKER RINGGIT DEBATE

let's TALK Op-Ed

The Malaysian investor abroad must first convert ringgits to a foreign currency for investment in the foreign country, and then later convert that foreign currency back to ringgits.

If in the meantime the ringgit becomes stronger vis-à-vis the foreign currency, then when the investor converts back to ringgits, the rate of return on that investment will be less than originally expected at the time it was made.

**Foreign investor in Malaysia (smiley):** However, a stronger ringgit is a blessing for a foreign investor putting monies into a Malaysian investment, as it will boost the returns of the said foreign investor.

That foreign investor converts from his domestic currency to ringgits for investment in Malaysia, while later planning to switch back to his domestic currency.

If, in the meantime, the ringgit grows stronger, then when the time comes to convert from ringgits back to the foreign currency, the investor will receive more foreign currency than expected at the time the original investment was made.

The reverse of all these cases of a stronger ringgit holds true in the case of a weaker ringgit, which is the situation now in Malaysia.

So what all this means is for a given weaker ringgit, three groups of economic actors experience bliss, while another three experience misery.

The same groups that enjoy bliss with a regime of weaker ringgit will experience misery with a stronger ringgit and vice versa with the other three groups in the case of a stronger ringgit.

So from the above explanation politicians who accused the government of not knowing what to do to "strengthen" the ringgit are barking up at the wrong tree.

If the government listens to them, then what will happen is, assuming their recommendations strengthen the ringgit, what we will see is a change of position – the smiley economic actors will become miserable, and the miserable will become the smiley emoticons.

Unless they can come up with proposals on how the miserable can be transformed into smiley actors with a stronger ringgit, without affecting the fate of those smiley actors who flourish under a weaker ringgit, their call for a stronger ringgit amount to nothing.

The government correctly sees the weakening ringgit as a non-issue as it will not lead Malaysia to an economic crisis as Finance Minister Tengku Dato' Seri Zafrul Tengku Abdul Aziz puts it.

The solution lies in mitigating the sufferings of those harmed by the weaker/stronger ringgit, and not in artificially appreciating/depreciating the ringgit.

What these politicians don't see is that it is not the weaker ringgit that is the problem but inflation.

# THE WRONG SLANT IN THE WEAKER RINGGIT DEBATE

let's TALK Op-Ed

It is fashionable nowadays in this era of financial crisis to see your country's currency stronger, and this has become somewhat populist, especially at a time of an election fever.

If these politicians come into power with their own idea of a stronger ringgit while remaining disconnected to the real issue of a weaker ringgit vis-à-vis a stronger ringgit, the country will go down the drain.

In economics, depreciation of currency that is 10% or less is an everyday occurrence that is not a cause for worry for as long as it does not take place on many consecutive days.

Ditto with less than 20% depreciation, which could happen once in a while.

But you've got to be very careful when there is a sudden 20% decline in the domestic currency because that is no longer a depreciation, but as good as a devaluation of the currency because it could lead to imported inflation for countries that are substantial importers.

This is because a sudden 20% decline in the domestic currency could result in imports costing 25% more, as a 20% decline means a 25% increase is needed to get back to the original price point.

One other thing the politicians clamouring for a stronger ringgit get it wrong is the slant of the story on the weaker ringgit.

The slant of the story is not that the ringgit is weakening against all other currencies, but rather mainly with the US dollar, the reserve currency of the world.

And the US like its allies in the EU is in a Catch-22 situation. The massive sanctions they imposed on Russia not only hurts Russia but boomerang to them as well in the form of an unprecedented spike in energy and food prices causing galloping inflation that was not seen in many years.

This high inflation can only be tamed with higher interest rate and the US Federal Reserve (Fed) is very focussed in sticking to aggressive rate hikes as inflation stays hot.

The Fed is expected to deliver a third straight 75-basis point interest rate hike this week, if not more, after a US government report showed that consumer prices did not ease as expected in August and price pressures appeared to broaden.

With an aggressive rate hikes approach, the US dollar is bound to appreciate again against all currencies in the coming days and weeks although the US is aware that such aggressive policies could result in the country going through a recession which will be contagious in spreading to other parts of the world.


# THE WRONG SLANT IN THE WEAKER RINGGIT DEBATE

let's TALK Op-Ed

But this is another Catch-22 story that will unfold much later and it would be interesting to watch when the US will stop this aggressive rate hikes policy in order to prevent recession.

Thus we can clearly see the angle or slant of the story as the ringgit weakens against the US dollar is then the story of almost all major currencies undergoing depreciation against the US dollar including the mighty Euro, the currency of the EU countries.

And thus the issue becomes is Malaysia the worst affected country in term of currency depreciation against the US dollar?

As pointed by Zafrul while the ringgit has depreciated by 7.5% against the US dollar since the beginning of 2022, many currencies in the region and developed countries have also fallen against the greenback.

"For example, the Japanese yen has slid 19.2%, the lowest in 24 years; the pound sterling has dropped 14.4%, the lowest in 37 years; and the euro has weakened by 11.7%, the lowest in 20 years," Zafrul said in a video posted on his social media page.

So Malaysia is doing well relative to all these countries as the ringgit's slide is the lowest among them all. Zafrul also stressed the ringgit has strengthened compared with the currencies of Malaysia's other trading partners.

Among others, the ringgit has risen by 14.2% against the Japanese yen, 8.2% versus the pound sterling, 4.5% vis-a-vis the euro, 3.9% compared with the New Zealand dollar, and 7.2% against the South Korean won.

"The important thing is, as an exporting country, the low ringgit against the US dollar has a positive effect on the country's export revenue.

"So do not look at just one aspect. Ask Malaysian exporters, they are all happy as their exported products have become more competitive," he said.

Additionally, economic fundamentals that have continued to strengthen are important in determining the robustness of the ringgit, the minister said.

"What are the proofs (that our economy is on a solid footing)? Firstly, Malaysia's gross domestic product (GDP) has grown for three consecutive quarters.

"The GDP grew by 3.6% in the fourth quarter of 2021, 5% in the first quarter of 2022 and 8.9% in the second quarter," he said.

Zafrul said the country's unemployment rate of 3.7% in July 2022, the lowest since the Covid-19 pandemic hit the country, is further proof that the country is not experiencing an economic crisis.


# THE WRONG SLANT IN THE WEAKER RINGGIT DEBATE

let's TALK Op-Ed

He also pointed to the Industrial Production Index, which rose by 12.5% year-on-year (y-o-y) in July 2022, and the sales value of the wholesale and retail trade which surged 41% to RM130.7 billion in the same month.

"For the first seven months of this year alone, wholesale and retail trade was valued at RM882.1 billion, 19% higher than last year," he said.
Zafrul also noted that the country's exports increased by 38% y-o-y to RM134.1 billion in July.
He added that net foreign investment in the local stock market has amounted to more than RM8 billion and net retail investment has reached RM1.8 billion year-to-date.

The country's inflation rate is also manageable at 2.8% for the first seven months of 2022 due to price control measures, particularly through the provision of subsidies of almost RM80 billion this year.

"So, it makes no sense for some to say, despite these positive indicators, that we are in an economic crisis," Zafrul said.

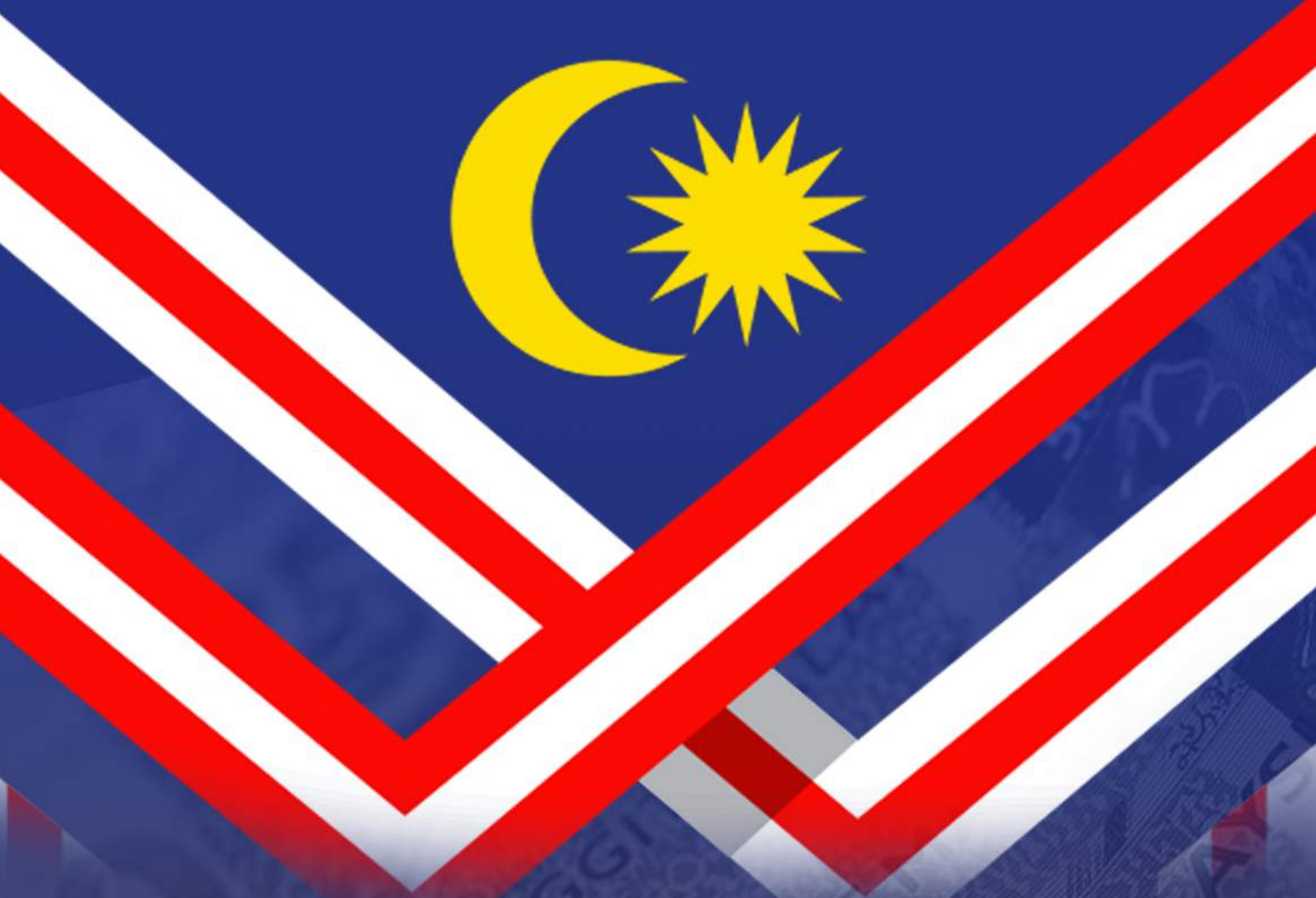
What was the reaction of these politicians who seems to be 'paralysed' by a weakened ringgit to Zafrul's statement?

Contemptuously accusing Zafrul of downplaying the ringgit's slide, and warning him that a downtrend against the greenback would affect Malaysians as it would see an increase in the cost of imported food, as if Zafrul is too naïve not to know this.

The problem of rising cost of imported food predates the current slide in the ringgit.

Even economists interviewed by Malaysiakini said the ringgit slide effect on daily life is minimal, although it's best to cut spending.

Regards,
Jamari Mohtar
Editor, Let's Talk!



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